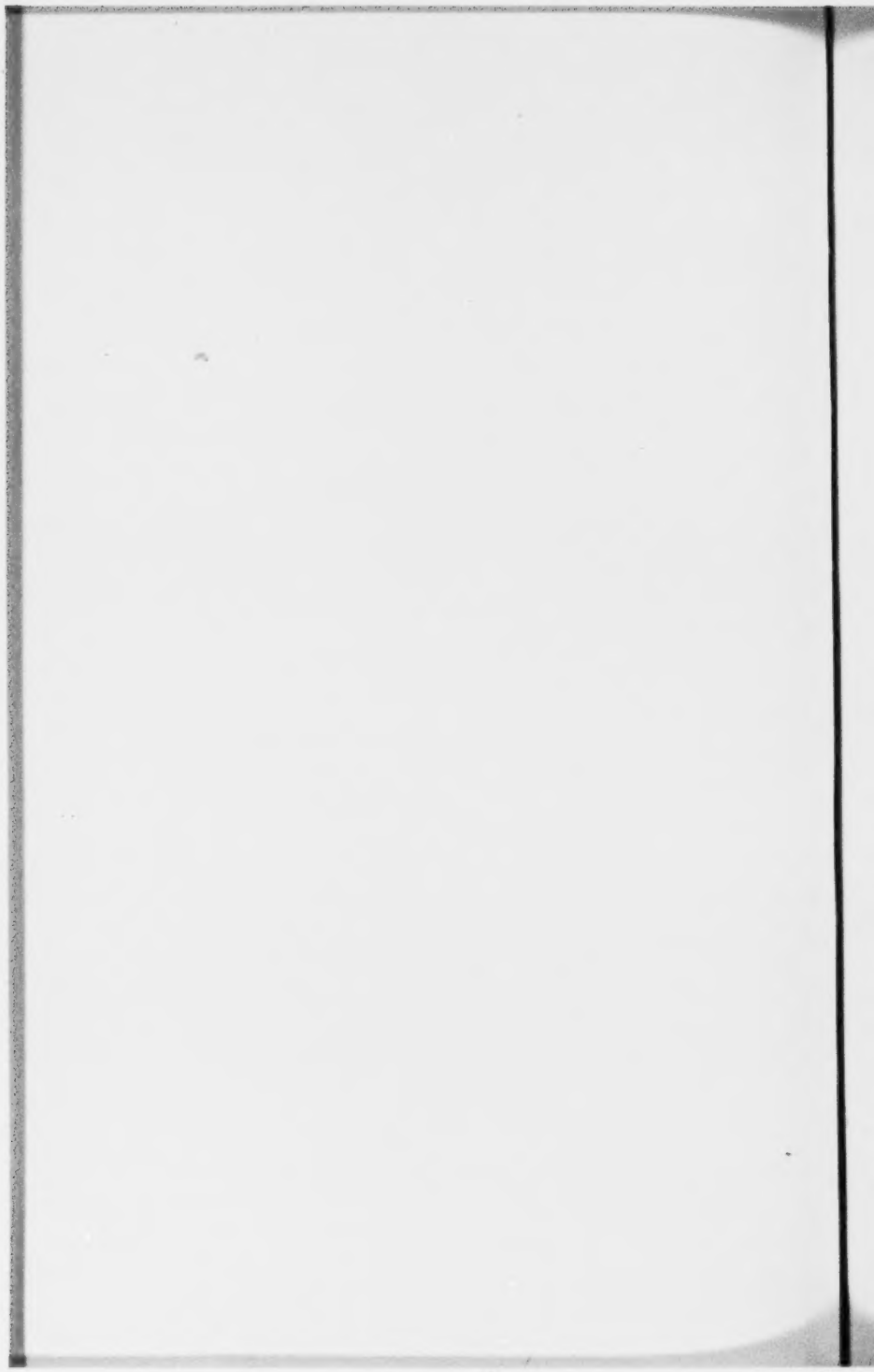

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Supreme Court of the United States

OCTOBER TERM, 1941

No. 266

IN THE MATTER

of

GEORGE A. CARDEN,

Bankrupt.

McCLAVE & COMPANY,

Petitioners,

GEORGE A. CARDEN, DANIEL LOEB, and Petitioning Creditors,

Respondents.

BRIEF OF RESPONDENTS IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI

LOUIS BOEHM,
Counsel for Respondents.

LOUIS BOEHM,
JOSEPH LEVINE,
ROBERT L. BOEHM,
of Counsel.

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BRIEF OF RESPONDENTS IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI

Statement

This brief is submitted in opposition to the petition for a writ of certiorari to review a decision of the Circuit Court of Appeals dated March 24, 1941, unanimously affirming an order of Hon. Alfred C. Coxe, District Judge, dated March 11, 1940 which denied petitioners' motion to dismiss an involuntary petition in bankruptcy (R. 4, 5).

The Facts

The petitioners are creditors of the bankrupt. The involuntary petition was filed on February 18, 1933 (R. 4) and was prosecuted to adjudication on December 21, 1939 (R. 32, 33). The principal ground of petitioners' motion

was that the petition does not state facts sufficient to confer jurisdiction upon the Court (R. 9). Petitioners' avowed purpose in seeking the dismissal of the petition in bankruptcy is to secure a priority over other creditors (R. 16, 25, 30). Petitioners, McClave & Company, are the only creditors seeking a dismissal of the petition. The bankrupt consented to adjudication (R. 5).

On June 5, 1939, petitioners caused the entry of two judgments against the bankrupt, one for $33,482.84, the other for $5,012.40 (R. 22, 23). Concededly, petitioners' claim of preference is not based upon these judgments (R. 30). The preference claimed by petitioners is based upon a judgment for $662,354.68 purchased by them for $100 at a receiver's sale on February 21, 1939 (R. 23). This judgment was recovered by one Irma Brown, by default, on July 21, 1937, on a promissory note given for a moral, but not legal, consideration (R. 15, 18). It is doubtful whether a judgment not based on a valid, legal claim is provable in bankruptcy.

On February 18, 1933, when the involuntary petition was filed in the court below, no receiver had been appointed, in any court, of the bankrupt or his property. On February 28, 1933, a receiver of the bankrupt's property was first appointed (R. 30).

Thereafter, on July 26, 1937, such receivership was extended to the $662,354.68 judgment now owned by petitioners, but which they had purchased for only $100 on February 21, 1939, almost two years later (R. 23).

Proceedings subsequent to the filing of the petition in bankruptcy were as follows: Sometime in 1939, several creditors and the bankrupt and his attorney held an informal meeting. It was there stated that on February 18, 1933, prior to the time when any claim of preference through the appointment of a receiver could have been made, an involuntary petition against the bankrupt had been filed. It was then suggested that if the petition be followed through and continued to adjudication, all of the

creditors could participate equally in whatever assets might be recovered, and in that way preferences would be avoided. Said creditors, together with the bankrupt, agreed to cooperate to the end that no particular creditor should obtain an undue advantage, and thereby deprive the other creditors of an equal share in whatever assets could be recovered. It was in pursuance of this understanding that the petitioning creditors decided to proceed with the involuntary petition which had been filed in 1933 (R. 19).

Several creditors in the same general position as the petitioners, but with unquestionably valid claims, have joined the other creditors in opposing petitioners' motion (R. 16).

This controversy, therefore, is really between a single creditor of the bankrupt, holding a doubtful claim purchased for a nominal consideration, and the other creditors, as to whether this creditor should be entitled to a preference over the other creditors in the distribution of the bankrupt's assets to the extent of $662,000, on a claim for which it paid the sum of $100 (R. 19).

In denying the motion to dismiss, Judge Coxe wrote the following opinion (R. 5):

> "Under Section 18-(b) of the present Bankruptcy act, creditors have no standing to contest the allegations of an involuntary petition; this is a radical change from the provision of the old section 18 (B). The Court clearly had jurisdiction in the present case, and the bankrupt does not question the adjudication.
>
> "The motion to vacate is denied."

On appeal, the Circuit Court of Appeals unanimously affirmed the decision of the District Court, with an opinion which is reported in 118 Fed. 2nd 677.

Substantially the only asset possessed by the bankrupt is a claim against the Government of the United States arising out of the sale of certain ships by the bankrupt and his partner during the World War. Enabling legislation was obtained permitting prosecution of the claim in the Court

of Claims, where, after voluminous testimony, the examiner reported in favor of allowing the claim for $2,800,000, but the Court of Claims disapproved the report and rejected the claim. Legislation is still being sought to permit the further prosecution of the claim by appeal to the Supreme Court, but to date has not been obtained (R. 20).

Summary of Argument

I. The District Court had jurisdiction of the petition in bankruptcy upon the filing thereof; the alleged defects contained therein were not jurisdictional.

II. The petition presents no question warranting an appeal to this Court.

III. In any event, under the Chandler Act petitioners have no standing to contest the allegations of the bankruptcy petition.

IV. Petitioners' right to attack the bankruptcy proceedings is governed solely by the Chandler Act. It is clearly practicable and equitable to apply the Chandler Act to this situation.

ARGUMENT

POINT I

The District Court had jurisdiction of the petition in bankruptcy upon the filing thereof; the alleged defects contained therein were not jurisdictional.

Petitioners' entire argument is based upon a single premise, wholly unsupported by authority, that the petition in bankruptcy was jurisdictionally defective because not filed until approximately one year after it had been signed by

the Petitioning Creditors. Petitioners cite three District Court cases in support of this facile assumption. None of these cases are in point upon this proposition.

On the other hand, the Circuit Court of Appeals, in its opinion herein, has carefully enunciated the applicable law. It stated at page 679 of its opinion (*In Re Carden,* 118 Fed. 2nd 677 [decided March 24, 1941]):

> "That brings us to the second question, always present, as to whether or not the order of adjudication was within the jurisdiction of the district court. As to that it is, of course, undoubted that the court had jurisdiction of the petition when filed and its jurisdiction of the bankrupt is clear. Whatever defects there may have been in the allegation of acts of bankruptcy at most made the petition demurrable because too general or because acts within four months of the filing were as of the date of signing wholly in the future and not accomplished facts. Such defects, however, could be cured by amendment and were not jurisdictional. The mere lapse of time between the filing of the petition and the service and adjudication could not deprive the court of jurisdiction.
>
> "At most, the order of adjudication might have been erroneous but that did not deprive the court of the jurisdictional power to make it. *In Re Shoesmith,* 135 Fed. 684. And, as we have seen, the appellant could not object to it for error merely. It must now be treated as a final order and all pertinent issues are res adjudicata. Compare, *Des Moines Nav. and R. R. Co.* v. *Iowa Homestead Co.,* 123 U. S. 552, 8 S. Ct. 217, 31 L. Ed. 202."

The petitioners complain that the Circuit Court of Appeals "treated this situation cavalierly". On the contrary, the Circuit Court's ruling is based upon law so well established that apparently the Court considered it unnecessary to cite authorities.

It is fundamental that upon the filing of a petition in bankruptcy containing the essential allegations, and the service of process, the Court obtains jurisdiction of the

subject matter and of the parties. *Denver First National Bank* v. *Klug,* 186 U. S. 202; *Lamp Chimney Co.* v. *Brass & Copper Co.,* 91 U. S. 656, 660; *In re First National Bank,* 152 Fed. 64; *In re Broadway Saving Trust Co.,* 152 Fed. 152; *In re 211 East Delaware Place Building Corp.,* 14 Fed. Supp. 96; *In re Tully,* 156 Fed. 634, 637; *In re Plymouth Cordage Co.,* 135 Fed. 1000, 1004; *United States ex rel. Weisman* v. *Brown,* 281 Fed. 657, 660; *In re Berner,* 3 A. B. R. 325 (U. S. D. C. N. D. Ohio).

In the case of *In Re First National Bank,* 152 Fed. 64 (C. C. A. 8th Cir.), the Court clearly expressed the foregoing principle as follows (pp. 68-9):

> "Jurisdiction of the subject matter and of the parties is the right to hear and determine the suit or proceeding in favor of or against the respective parties to it. * * * *A defective petition in bankruptcy, or an insufficient complaint at law, accompanied by proper service of process upon the defendants gives jurisdiction to the court to determine the questions involved in the suit, although it may not contain averments which entitle the complainant to any relief.* * * * *The facts which conditioned the jurisdiction of the court were the filing of the petition and the service of the subpoena. In re Plymouth Cordage Co.,* 135 Fed. (2) 1000, 1004; 68 C. C. A. 434, 438."

From this it clearly follows that the District Court had jurisdiction of the petition in bankruptcy herein in the first instance. Any defect in the pleading of said petition was not a jurisdictional defect. In and of itself it did not preclude an adjudication. *Bradley* v. *Huntington, et al.,* 277 Fed. 948 (C. C. A., 2nd Cir.); *In re Shoesmith,* 135 Fed. 684; *In Re Middle West Utilities Co.,* 70 Fed. (2) 825; *In Re S. W. Strauss & Co.,* 67 Fed. (2) 605; *In Re 211 East Delaware Place Bldg. Corp.,* 14 Fed. Supp. 96; *Conway* v. *German,* 166 Fed. 67; *In Re Plymouth Cordage Co.,* 135 Fed. 1000.

In the instant case, the allegations of the petition were admitted by the bankrupt when he defaulted. Under the

authority of the foregoing cases, the Court had jurisdiction and the subsequent adjudication was therefore proper.

It is well settled that verification of a petition is a matter of form not affecting the jurisdiction of the Court, and, if the bankrupt pleads to the merits without objecting to the form of the petition (or, as in this case, defaults), he waives any defects in the verification. *In re O'Brien,* 78 F. (2) 715 (C. C. A., 2nd Cir.); *Leidigh Carriage Co.* v. *Stengel,* 95 Fed. 637; *Rosaly* v. *Gonzalez,* 106 Fed. (2) 169, 171; *Sabin* v. *Blake M'Fall Co.,* 223 Fed. 501; *In Re Plymouth Cordage Co.,* 135 Fed. 1,000; *In Re Vastbinder,* 126 Fed. 417; *In Re McNaughton,* 16 Fed. Cas. 323.

In *In Re O'Brien,* 78 F. (2) 715, *supra,* the appellant contended that the debtor's petition had not been verified, and that therefore, the court had no jurisdiction. The Court said (p. 716):

> "The Statute does not expressly declare that the debtor's petition must be verified but we shall assume, as does official Form No. 65 (11 U. S. C. A. following section 53), that verification is required. But this is merely a procedural matter and the absence of a proper verification is not a jurisdictional defect, as has been frequently held with respect to petitions filed under other provisions of the Bankruptcy Act" (citing cases).

In the instant case the petition was verified. The alleged irregularity of the verification is not a jurisdictional defect. Even had there been no verification whatever, still, under the authorities, the defect would not have been jurisdictional.

Diligent research on our part has brought to light only one reported case where a petition in bankruptcy was attacked because a substantial interval of time elapsed between the verification of the petition and the filing thereof. In *In re Berner,* 3 A. B. R. 325 (U. S. D. C. N. D. Ohio, Eastern Div. in Bkcy.; Harold Remington, Referee) a voluntary petition filed two months after verification was held

jurisdictionally proper by Referee Remington who said, pages 328-329:

> "Concerning the fact that the petition and schedules were not sworn to at the time of filing, it seems to the referee that these are not jurisdictional defects but that the same could and should be cured by amendment. * * * The only case the referee has been directed to or has discovered which considered the effect of an interval elapsing between the verification and the filing of petition in bankruptcy is *In re: Abrahams,* Federal Cases No. 20 and this case inferentially is opposed to the contention of there being lack of jurisdiction upon that ground."

The petitioners, in attempting to obtain a dismissal of the petition herein, have sought to draw an analogy between their application to dismiss an involuntary petition and the right of creditors under the old act to attack a voluntary petition in certain cases (petitioners' brief, pp. 12-13). This argument must fail because, even in the cases cited by petitioner, the creditor would have been barred from attacking a petition had the defect been "less than jurisdictional" (petitioners' brief, pp. 12-13). The rule in those cases was that although a creditor might oppose an adjudication where jurisdictional elements were lacking, he could not do so where jurisdictional elements existed. *Re Fox West Coast Theaters,* 25 F. Supp. 250, affd. 88 F. (2) 212, cert. denied, *Tally* v. *Fox,* 301 U. S. 710, rehearing denied 302 U. S. 772. *There was no jurisdictional defect here.* Only the debtor himself could have attacked the form of the petition. As this Court said in *Royal Indemnity Co.* v. *American Bond and Mortgage Co.,* 289 U. S. 165 cited by petitioner:

> "Creditors have no standing to plead statutory requirements not intended for their protection."

The debtor's default was an admission of the allegations of the petition, and adjudication of bankruptcy properly followed (*Bradley* v. *Huntington,* 277 Fed. 948, 950).

POINT II

The petition presents no question warranting an appeal to this Court.

Reduced to fundamentals, the petition herein presents but one question, namely the sufficiency of a petition in bankruptcy which has been filed more than four months after its verification by the petitioning creditors. That the District Court had jurisdiction of said petition has already been shown.

The petitioners therefore, in reality, seek a re-determination of the sufficiency of the petition in bankruptcy. Such a question is not one which this Court will review. *Magnum Import Co.* v. *Coty*, 262 U. S. 159, 163; *Forsyth* v. *Hammond*, 166 U. S. 506, 514; *Amer. Construction Co.* v. *Jacksonville Railway*, 148 U. S. 372, 383; *In Re Woods*, 143 U. S. 202, 206; *Lau Ow Bew, Petitioner*, 141 U. S. 583, 587.

As this Court declared in *Forsyth* v. *Hammond*, 166 U. S. 506, 514, 515:

> "And further, that while this power (to review) is co-extensive with all possible necessities and sufficient to secure to this court a final control over the litigation of all Courts of Appeal, it is a power which will be sparingly exercised, and only when the circumstances of the case satisfy us that the importance of the question involved, the necessity of avoiding conflict between two or more Courts of Appeal, or between Courts of Appeal and the courts of a State, or some matter affecting the interests of this nation in its internal or external relations, demands such exercise."

Chief Justice Taft stated the proposition most emphatically in *Magnum Import Co.* v. *Coty*, 262 U. S. 159, 163, as follows:

> "The jurisdiction was not conferred upon this Court merely to give the defeated party in the Circuit Court

> of Appeals another hearing. Our experience shows that eighty per cent of those who petition for certiorari do not appreciate these necessary limitations upon our issue of the writ."

Clearly the formal sufficiency of a petition in bankruptcy is not a matter of such grave public importance as to require the time and attention of this Court.

POINT III

In any event, under the Chandler Act petitioners have no standing to contest the allegations of the bankruptcy petition.

The old Bankruptcy Act, Section 18b, provided:

> "A bankrupt *or any creditor* may appear and plead to the petition within five days after the return date or within such further time as the court may allow."

The Chandler Act, Section 18b, retains the language of the old Section 18b, but omits the words *"or any creditor"*.

Section 59f of the old Bankruptcy Act provided:

> "Creditors, other than original petitioners, may at any time enter their appearance and join in the petition *or file an answer and be heard in opposition* to the prayer of the petition."

Section 59f of the Chandler Act again retains the language of the old section 59f, but omits the words "or file an answer and be heard in opposition to the prayer of the petition."

The deletions by Congress from the Chandler Act of these provisions of the old Bankruptcy Act which permitted creditors to be heard in opposition to a petition for involuntary bankruptcy were patently made for one purpose, namely, to take away from them that power which the old Bankruptcy Act had conferred upon them (and

which they had notoriously abused), and to reserve such power solely to the bankrupt. Any other interpretation would render these purposeful omissions meaningless. The opinion of the Circuit Court of Appeals (*In re Carden*, 118 Fed. 2nd 677) gave full expression to this view, holding at page 679:

> "The old Act provided in Sec. 18 (b) that the bankrupt or any creditor might appear and plead to the petition within five days after the return date or within such further time as the court might allow. In Sec. 18 sub. b of the Chandler Act this provision was changed by omitting the words 'or any creditor'. Similarly, Sec. 59 sub. f of the old Act, 11 U. S. C. A. § 95, sub. f, gave creditors, other than the original petitioners, the right to enter their appearance at any time and join in the petition or file an answer and be heard in opposition to the prayer of the petition. In Sec. 59 sub. f of the Chandler Act the words 'or file an answer and be heard in opposition' were left out. *These omissions make it clear that Congress did not intend to give a statutory right to creditors to contest the allegations in an involuntary petition.* We must take it for granted that the district court held that the application of the Chandler Act was feasible since it was actually applied and there is no question as to the soundness of that ruling."

The argument of the petitioner that the failure of Congress to specifically confer rights upon creditors to contest an adjudication under the Chandler Act was due to its reliance upon the reserve power of the bankruptcy court to accord such a status to them (p. 14, Petitioner's brief) is unsound. It is fully answered by the report of the House Committee on the Judiciary which discloses the legislative purpose behind these new sections:

> "The report of the House Committee on the Judiciary (Report No. 1408, 75th Congress, 1st Session), in referring to 'Amendments to increase efficiency in administration' states in part as follows:

> "'*The right of creditors to file answer eliminated.* The right of creditors to file an answer and oppose the petition has been eliminated in the amendment to Section 18 b, and Section 59 f has been changed to correspond to this amendment. A creditor should not be permitted to oppose an adjudication; invariably the motive of such creditor is to protect a preference or to retain some other undue advantage at the expense of the other creditors contrary to the fundamental purpose of the act—an equitable distribution among all creditors.'"
>
> *1 Prentiss-Hall Bankruptcy Service,* 1204.

The Judiciary Committee's report aptly describes the avowed motive of the petitioners herein in opposing the adjudication, *i. e.,* to "protect a preference or to retain some other undue advantage at the expense of the other creditors, contrary to the fundamental purpose of the act—an equitable distribution among all creditors". And it was specifically to remedy that abuse of the right of opposition by creditors under the old Act that Congress in the Chandler Act withheld that right from them.

To allow petitioners to oppose the adjudication here, and to achieve their admitted purpose, would nullify the present statute and its expressed legislative intent.

POINT IV

Petitioners' right to attack the bankruptcy proceedings is governed solely by the Chandler Act. It is clearly practicable and equitable to apply the Chandler Act to this situation.

Petitioners' claim that they possess a general equitable right under the reserve power of the Court to attack the adjudication, was fully discussed and clearly answered by the Circuit Court of Appeals in its opinion (*In Re Carden,* 118 Fed. 2nd 677). The Court declared at page 679:

> "Since there is no longer any express statutory right given creditors to contest an adjudication upon an involuntary petition in bankruptcy, the right, if any, of creditors to make such a contest must rest upon general principles of equity applicable in bankruptcy proceedings. It is true that such principles will govern action in a bankruptcy court when not in conflict with the statute. Securities Comm. v. U. S. Realty Co., 310 U. S. 434, 457 60 S. Ct. 1044, 84 L. Ed. 1293. But where there has been an amendment to the statute whereby such right formerly existent has been withdrawn, there has been the equivalent of a statutory denial of the right and any action under general principles of equity contrary thereto would be contrary to the statute and so erroneous. Consequently, the appellant was without standing to question the sufficiency of the petition."

Notwithstanding petitioners' appeals for equity it is apparent that what they seek to accomplish is inequity. Petitioners concede that the sole purpose of their proceeding herein is to obtain a preference for their judgment of over $662,000 (purchased for $100) and perhaps thereby obtain all of the realizable assets of the bankrupt, at the expense, and perhaps the utter exclusion, of all the other creditors. It is axiomatic that the bankruptcy statutes look primarily to equitable distribution among all creditors. "In the disposition of property among creditors, equality is equity." *Bank* v. *Sherman,* 101 U. S. 403, 406.

There is no difficulty encountered here in applying the new provisions of the Chandler Act depriving creditors of the right to oppose an involuntary petition. Petitioners actually had no claim at all against the bankrupt until February 21, 1939, some six months after the effective date of the Chandler Act, when it purchased a judgment for $662,354.68 for the sum of $100. The "vestedness" of its right is more imaginary than real.

The application of the Chandler Act to the instant case is quite simple, fair and feasible. It affects only a prior existing procedural right. It was applied here merely by

denying the creditor's motion to dismiss. It did not impair, impede or complicate the efficient administration of the estate. Equity and justice require that the Chandler Act be applied herein, to the end that there may be a rateable distribution among all creditors.

Conclusion

No question has been presented by the petition for review by this Court. Petitioners' entire argument rests upon an alleged insufficiency in a petition in bankruptcy which they assume, without citing any applicable legal authority in support thereof, deprived the court completely of its jurisdiction to adjudicate the defendant a bankrupt.

Petitioners' attack upon this adjudication is precisely the evil which the Chandler Act was designed to and did prohibit, namely the attempt by a single creditor to obtain an undue advantage at the expense of the other creditors. The intention of Congress to eliminate such practice is manifest in the Chandler Act, and in its legislative history.

We submit, therefore, that the petition should be denied.

Respectfully submitted,

LOUIS BOEHM,
Attorney for Respondents.

LOUIS BOEHM,
JOSEPH LEVINE,
ROBERT L. BOEHM,
of Counsel.